

UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

San Diego Gas & Electric Company,  
Complainant,

v.

Sellers of Energy and Ancillary Services  
Into Markets Operated by the California  
Independent System Operator and the  
California Power Exchange,

Respondents.

Docket Nos. EL00-95-000  
EL00-95-002  
EL00-95-003

Investigation of Practices of the California  
Independent System Operator and the  
California Power Exchange

Docket Nos. EL00-98-000  
EL00-98-002  
EL00-98-003

Public Meeting in San Diego, California

Docket No. EL00-107-000

Reliant Energy Power Generation, Inc.,  
Dynegy Power Marketing, Inc.,  
and Southern Energy California, L.L.C.,  
Complainants,

v.

California Independent System Operator  
Corporation,

Respondent.

Docket No. EL00-97-000

California Electricity Oversight Board,  
Complainant,

v.

All Sellers of Energy and Ancillary Services  
Into the Energy and Ancillary Services Markets  
Operated by the California Independent System  
Operator and the California Power Exchange,  
Respondents.

Docket No. EL00-104-000

California Municipal Utilities Association,  
Complainant,

v.

All Jurisdictional Sellers of Energy and Ancillary

Docket No. EL01-1-000

Services Into Markets Operated by the California  
Independent System Operator and the  
California Power Exchange,

Respondents.

Californians for Renewable Energy, Inc. (CARE),  
Complainant,

v.

Independent Energy Producers, Inc., and All  
Sellers of Energy and Ancillary Services Into  
Markets Operated by the California Independent  
System Operator and the California Power  
Exchange; All Scheduling Coordinators Acting  
on Behalf of the Above Sellers; California  
Independent System Operator Corporation; and  
California Power Exchange Corporation,

Respondents.

Docket No. EL01-2-000

Puget Sound Energy, Inc.,

Complainant,

v.

All Jurisdictional Sellers of Energy and/or Capacity  
at Wholesale Into Electric Energy and/or Capacity  
Markets in the Pacific Northwest, Including  
Parties to the Western Systems Power Pool  
Agreement,

Respondents.

Docket No. EL01-10-000

(Issued January 18, 2001)

Hoecker, Chairman, concurring further:

Today I take the unusual step of issuing an addendum to my concurrence of January 4, 2001, to reemphasize the need to find a comprehensive solution to California's deepening energy crisis. This year, energy is costlier in most regions of the country, but in California a cavalcade of misjudgments and bad luck have caused a genuine economic and social crisis. The situation has deteriorated further since early January. Negotiations over long term contracts have reached impasse, notwithstanding many hours of tough talk in Washington and the herculean (but ultimately inadequate) efforts of state legislators to buttress sagging utility creditworthiness and to find a sustainable retail rate compromise. California's reserves have evaporated this winter as recurrent plant outages continue and weather forced valuable units off line. Yesterday, the ISO had no choice but to order rolling blackouts in northern and central California in order to prevent a system collapse. So, to the financial crisis, we now

add a serious threat to human welfare. With consumer rates frozen below cost (and below 1996 levels), with generators wary of making sales to entities probably unable to pay for power generated at unseasonably (and even historically) high cost, and with no plan to amortize existing utility arrearage, Southern California Edison and Pacific Gas & Electric stand at the brink of insolvency. For following the state's restructuring law, they may go bankrupt. Moreover, with only minimal forward contracting and utilities still subjected to high PX spot market prices for their "net short" position, the Commission's plan to diminish and discipline the spot market remains unrealized. Amidst a severe power shortage, conspiracy theories, resistance to more realistic rates, and calls for palliative price caps continue to obscure the issues and delay solutions.

Perhaps bankruptcy can be averted. If it cannot, perhaps it will force the debtors, creditors, and state officials to address the financial problems of utilities in a new light, without recrimination and posturing. Will the time for positive planning then be at hand? Let's be realistic. Chapter 11 will not recast or dispose of the California's serious ratepayer and public interest issues. It will not eliminate the power or responsibilities of regulators. It will not enable the system to create one additional electron. And, while it will not necessarily reduce service reliability or render utilities inoperable, neither will it improve electricity service functions, at least without the kind of technical planning and difficult choices we have repeatedly urged. Wall Street and consumers share one critical trait: without a reasonable, technically defensible, and comprehensive set of solutions to such crises, they have no basis for confidence that problems can or will be managed or confidence to support investment on one hand and political forbearance on the other.

I take the liberty, at this moment of my departure from office, to reiterate what must be done here and in California, and perhaps to puzzle about why this is so hard.

A. The State Needs To Work With, Not Against, FERC

The Commission's December 15, 2000, order must be implemented expeditiously. The PX has yet to comply with the new pricing procedures which limit the impact of the single price auction. As a result, prices produced by the PX are not in compliance with the order (i.e., all sales continue to be priced at the highest cost rather than at the \$150 breakpoint for bids at or below \$150 or at their bid price if above). This confuses both the market and public policymakers. It will lead either to increases in the cost of power to buyers above that permitted by the December 15 order or retroactive recalculation of the rate using the \$150 limit to enforce compliance. The potential for prices above the level allowed in the December 15 order has further jeopardized the financial status of California utilities.

B. Manage The Risks.

Forward contracts have to be negotiated as soon as possible, with or without a bankruptcy. Delay simply increases the cost to consumers in the long run, and many opportunities for lower cost forward contracts have already been lost in the false expectation that more time would lead to lower, not higher, prices. Sooner or later, retail prices must provide for recovery of legitimate costs incurred to meet the needs of consumers. While there may be multiple ways to blend rates over time to lessen ratepayer burdens and defer recovery, an arbitrary bottom-line solution cannot be prescribed without regard to costs, the availability of units, and the dynamics of the regional electric system.

C. Regulators Must Regulate.

New techniques for monitoring and mitigating market power must be designed expeditiously, in accordance with our order. I believe that the exercise of market power is not unlawful in and of itself. There are clearly circumstances in which market power is used for more than taking advantage of revenue maximizing opportunities. If the market permits the imposition of unjust and unreasonable rates, these circumstances must be identified and penalties applied -- based on more than supposition. Consumers are entitled to fair rates and suppliers are entitled to know the standards to which they will be held and the consequences for failing to adhere to those standards. Those consequences must be implementable in real-time; after-the-fact refunds are not a suitable foundation for remedying market power going forward, even though we should pledge to post-October 2, 2000, refund obligation timely and fairly. All this is this Commission's responsibility, but the CPUC and other appropriate California officials can demonstrate their willingness to work constructively with us. We can start down a new road together

beginning on January 23, 2001, when we convene an important technical conference on California's market problems.

D. More Police Work

Investigations of outage events must be completed, not only for the purpose of identifying past behavior that may have been unlawful, but also for the purpose of identifying future market monitoring techniques and to identify opportunities for coordinating planned outages throughout the regional market to bolster reliability.

#### E. New Regional Procedures

In addition to prompt review of prices for transactions during 2001, the Commission must adopt expeditious procedures to review prices occurring between October 2, 2000, through the end of 2000. Unless and until the Commission determines the just and reasonable rate for all transactions under occurring during the refund period, the refund obligation of suppliers cannot be resolved.

#### F. Separating Markets and Politics

California's recent legislation changing the ISO governance board reflects, in my view, another triumph of expedience over cooperation and understanding of the electric system. While stacking the board of a FERC-jurisdictional public utility with state political appointees may not raise ire in California, it is an unacceptable intrusion - - not unlike the mistakes of AB1890 - - into federally regulated power markets. Such a measure surely imperils the California ISO's eligibility as an RTO under Order No. 2000. Because the state is now clearly a market participant, the independence of the board is bound to be compromised. Consequently, the state's decisions are no longer entitled to the kind of deference we have accorded it since AB 1890. More than that, this action evinces a bald disregard for federal jurisdiction and a rejection of cooperative solutions. On December 15, the FERC delayed making a final ruling on governance in order to consult with state authorities on this matter. This is their apparent response. I do not think the legislation offers any meaningful chance to negotiate a deal. Therefore, I recommend that the Commission seek to enjoin this technically flawed and unlawful usurpation of its authority.

#### G. Price Caps Revisited.

The Commission must be prepared to support plans that constructively and comprehensively address the situation. As I stated in my earlier concurrence, I support a "time out" from current wholesale prices, if they are part of a work-out plan that has a chance of garnering support from all parties and achieving an equal sharing of the pain. Without that, price caps will only jeopardize reliability, mask problems temporarily, and deter or destroy any chance to solve the long-term supply challenge.

#### Conclusion

Urgency is a must. I am persuaded that California's utilities can still be withdrawn from the brink. But their descent into Chapter 11 does not materially alter the need to act to devise a coordinated plan of action. We have reached this stage of growing crisis through a series of acts of

short-term thinking and now the desperation is palpable. We cannot, however, keep moving from one failure to the next, with no agreed-upon objectives. The Governor's stated plans are unrealistic and ours cannot be fully implemented without his help. Time to put down the guns.

The long-term health of California wholesale markets turns on access to regional markets that are competitive and efficient and which eliminate existing barriers to regional reliability and coordination. Participation in a regional transmission organization (RTO) will provide the best opportunity to bring back reliability and rate stability to California consumers quickly. I urge state policymakers to reject the false illusion that going it alone will serve the interests of California consumers. Instead, policymakers from all Western states should work together to maximize the benefits of the regional grid and regional market for all Western consumers. It is in our collective interest and in the interest of the Nation's economic welfare, to begin the difficult process of developing a New Electric System capable of meeting unanticipated demand, serving customers in an economic and environmentally acceptable manner, and generating creativity and service innovation along with electricity.

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James J. Hoecker  
Chairman